Supreme Court, U.S.
FILED

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No. _____

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1999

Jerry Krim, on behalf of himself and all others similarly situated, and Harold L. Harris, individually and as Trustee of Mazel, Inc. Profit Sharing Plan,

Petitioners

v.

A. Robert Abboud, Frank C. Cihak, Robert D. Richley, Richard Rice, William M. Arnold, Donaldson Lufkin & Jenrette Securities Corp., C. Ivan Wilson, Robert W. Brown, Daniel C. Arnold, Robert Rice, Robert H. Allen, J. Evans Attwell, William T. Butler, M.D., J.A. Elkins, Jr., James H. Evans, C. Jackson Grayson, Jr., Robert N. Murray, Ralph S. O'Connor, and Margaret S. Wilson,

Respondents

On Petition For Writ Of Certiorari
To The United States Court Of Appeals
For The Fifth Circuit

PETITION FOR WRIT OF CERTIORARI

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February 2000

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QUESTIONS PRESENTED FOR REVIEW

1. Whether a plaintiff found by the district court not to have suffered an injury in fact at the time of filing his original complaint can nevertheless be cured of the alleged deficiency through a subsequent amended complaint in which he can assert an injury in fact, thus allowing the case to proceed.

2. Whether a guardian may sue on behalf of a minor ward without joining the ward in the lawsuit, either pursuant to Fed. R. Civ. P. 17, or under the exception permitting a litigant to bring an action on behalf of a third party under certain circumstances.

3. Whether, in the class action context, a district court should be required to rule as to plaintiff's standing early in the litigation process, so as to limit the risk that the statute of limitations will expire as to other class members if the original complaint is dismissed for plaintiff's lack of standing.

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Jerry Krim and Harold L. Harris respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Fifth Circuit and the United States District Court for the Southern District of Texas, Houston Division, in this case.

OPINIONS BELOW

The opinion of the court of appeals (App., *infra*, 1a - 2a) and the judgment and opinion of the district court (App., *infra*, 3a -11a) are unreported.

JURISDICTION

The court of appeals entered its judgment on November 8, 1999 (App., *infra*, 1a). The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

Rule 15(a) of the Federal Rules of Civil Procedure is involved in this case, and states as follows:

> Rule 15. Amended and Supplemental Pleadings
>
> (a) Amendments. A party may amend the party's pleading once as a matter of course at any time before a responsive pleading is served or, if the pleading is one to which no responsive pleading is permitted and the action has not been placed upon the trial calendar, the party may so amend it at any time within 20 days after it is served. Otherwise a party may amend the party's pleading only by leave of court or by written consent of the adverse party; and leave shall be freely given when justice so requires. A party shall plead in response to an amended pleading within the time remaining for response to the original pleading or within 10 days after service of the amended pleading, whichever period may be the longer, unless the court otherwise orders.

STATEMENT

This Petition arises from the dismissal of a class action brought in the United States District Court for the Southern District of Texas, Houston Division, affirmed on appeal to the United States Court of Appeals for the Fifth Circuit. The jurisdiction of the district court was invoked under 28 U.S.C. § 1331 as a federal question under the Securities Act of 1933 (the "1933 Act"), the Securities Exchange Act of 1934 (the "1934 Act"), and Rule 10b-5 of the Securities and Exchange Commission (17 C.F.R. § 240.10b-5) together with pendent claims under the Texas Business & Commerce Code and the common law.

Plaintiff Jerry Krim ("Krim") filed his original complaint on July 16, 1990 alleging violations by First City Bancorporation of Texas, Inc. ("First City"), its officers and directors, and its financial advisor Donaldson, Lufkin & Jenrette ("DLJ") of Sections 10(b) and 20 of the 1934 Act and Sections 11, 12(2) and 15 of the 1933 Act.

Krim had invested in First City stock in 1988 through his wife's purchase of shares as custodian for their son, who was then a minor (Doc. 171 at 4). In addition to the shares already owned by the Krim family, Krim purchased additional shares of First City on July 19, 1990, three days after filing his complaint. Following Krim's purchase on his own account and continuing for over two years thereafter additional wrongdoing was committed by principals at First City and others, and such wrongdoing was kept secret from the investing public by the officer and director defendants. Thus, Krim was the victim of further fraudulent activity that took place after his purchase of First City stock on July 19, 1990, the existence of which he could not have known about. Similarly, petitioner Harold L. Harris ("Harris"), who was added to the complaint on May 24, 1991, was also harmed by such later instances of the defendants' wrongdoing.

The complaint sets forth specific allegations that the defendants caused injury to the First City shareholders by making material false and misleading statements in the public financial statements of First City with respect to the true financial condition of the company. The complaint alleged that the defendants painted a materially false and overly optimistic picture of First City's financial condition and failed to inform the shareholders about the risky loans First City was actually making (Doc. 132 at 14-21) and about the poor condition of the assets held by the First City Collecting Bank

("Collecting Bank"), an entity formed in January 1988 to liquidate all bad loans made by First City prior to its restructuring in 1988 (Doc. 132 at 21-24).

There is ample evidence that there was criminally fraudulent activity at First City. However, respondent Frank C. Cihak ("Cihak") has been the only person directly related to the bank who has been made to pay for the egregious conduct at First City during the class period, April 19, 1988 through October 30, 1992 (the "Class Period"). Cihak was convicted and is now serving sentences on two separate federal indictments totaling over 70 counts of bank fraud, money laundering and related activities. *U.S.A. v. Cihak, et al.*, Case No. 4:93cr00119 (S.D. Tex.); *U.S.A. v. Cihak, et al.*, Case No. 4:95cr00027 (S.D. Tex.).

Much of the criminal activity of which Cihak was accused in the indictments is also alleged in the latest version of the complaint, the Seventh Amended Complaint filed on October 21, 1997 (Doc. 132, the "Complaint"). The criminal activities fraudulently diverted at least $10 million in assets from First City during the Class Period. The Complaint alleges further that these criminally fraudulent acts were participated in, known about and covered up by the other respondents herein, namely, A. Robert Abboud, all the officers and directors at the time, and DLJ. In addition, the outside counsel to First City, the Chicago law firm Keck, Mahin & Cate, was directly involved in the fraud.[1]

There is no question that the investors who purchased First City stock during the Class Period had no knowledge, or access to knowledge, of the undisclosed criminal and fraudulent activities, and lost a great deal of money. Claims submitted by class members to the United States Bankruptcy Court for the Northern District of Texas, Dallas Division (*In re First City Bancorporation of Texas, Inc.*, Case

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[1] Although and Keck, Mahin & Cate and its then-partner Henry Landan were included as defendants on the Seventh Amended Complaint, the case against them was severed by order of the district court dated March 10, 1998 (Doc. 170), when Keck, Mahin & Cate filed for chapter 11 protection in the United States Bankruptcy Court in Chicago, Illinois.

No. 392-39474-HCA-11, Chapter 11) for their losses in connection with the allegations in the Complaint total approximately $375 million, of which only $11 million was recovered by the class by settlement reached with the debtor First City only.

Procedural History

The original complaint was filed on July 16, 1990 by plaintiff Krim. Several amended versions of the complaint were filed in the ensuing months as more and more information about the on-going fraud surfaced, and the defendants filed several corresponding motions to dismiss. By order entered March 28, 1991 (Doc. 52), the district court denied *all* the defendants' motions to dismiss up to that point (Doc. Nos. 8, 9, 37, 46, 49).

In addition to being rife with errors of procedure and law, the district court's Opinion contains a grave factual error. The Opinion relates that Krim filed a Sixth Amended Complaint without leave of the court to amend and "in violation of the court-ordered deadline of April 8, 1991 for joining new parties and amending pleadings" (App. *infra*, 5a), apparently referring to a scheduling order entered July 16, 1990 (Doc. 3). However, the district court overlooked and failed to recall its order entered March 28, 1991 (App., *infra*, 12a-13a), which superseded the July 16, 1990 scheduling order and states as follows:

> (c) The defendants' motion to dismiss the plaintiff's fourth and fifth complaint (instrument #37, 46, and 49) are DENIED without prejudice and the need to refile same. In this regard, *the plaintiff is ORDERED to file a Sixth Amended Complaint, within 60 days* expressly satisfying the particularities required to establish a claim for securities fraud and for claims under the Securities Act of 1933 or the Securities Exchange Act of 1934.

(App., *infra*, 13a, emphasis supplied.) The plaintiff filed the Sixth Amended Complaint on May 24, 1991 (Doc. 62), in compliance with the 60-day time limit ordered by the district court.

The district court based its rejection of Harris as a plaintiff on its utterly erroneous view that the Sixth Amendment Complaint was filed without leave of the court. The effect of this error has been unjustly devastating to the entire class.

In connection with the plaintiffs' motions for class certification,

the district court stated that it twice denied class certification in this case and conditionally approved class certification only for purposes of a proposed settlement (App., *infra*, 6a). The proposed partial settlement of $20 million failed due to First City's chapter 11 proceedings *(see infra)*. However, the two denials, by orders entered March 28, 1991 (Doc. 52) and May 9, 1991 (Doc. 59), were both made *prior to the filing of the Sixth Amended Complaint, and therefore never considered whether plaintiff Harris, who joined on May 24, 1991, would be an adequate class representative.* Thus, the district court never entertained the adequacy of plaintiff Harris for class certification purposes, *even though Harris was added to the case in direct response to the court's order of March 28, 1991 to amend the complaint.*

The district court allowed the litigation to proceed on the Sixth Amended Complaint for well over a year, taking the defendants' motions to dismiss the Sixth Amended Complaint "under advisement" (Doc. 66, Order dated July 8, 1991), and allowing Krim and Harris to proceed with discovery in accord with the previously entered scheduling order and amendments thereto (Doc. 3, 76, 80, 85, 89), tolling statutes of limitations with respect to certain defendants (Doc. 67), presiding over a settlement conference on September 14, 1992 (Doc. 93), and two days later even entering an Order With Respect to Notice of Conditional Class Certification, Preliminary Settlement Approval, and Settlement Hearing (Doc. 94), in response to a joint motion of the plaintiffs and the settling defendants. A settlement conference was set for November 24, 1992 (Doc. 94).

In addition, years later by order dated June 16, 1997 (Doc. 124), the district court granted leave to the plaintiffs to file a *seventh* amended complaint.

The November 1992 settlement was aborted when, on October 30, 1992, the federal and state bank regulators seized First City's operating banks declaring them insolvent. First City filed a petition under chapter 11 in bankruptcy a short time later. On December 17, 1992, the District Court declared First City under protection of the automatic stay in bankruptcy, and stayed the entire litigation as to *all defendants* (Doc. 104), instead of applying the stay to the debtor alone.

Two years later, on December 15, 1994, the parties filed a joint motion for a status conference (Doc. 113), which the District Court

denied (Doc., no number, December 20, 1994). On June 7, 1995, with a plan of reorganization of First City having just been confirmed by the bankruptcy court in Dallas on May 31, 1995 (the effective date was July 3, 1995), the plaintiffs moved the district court to reinstate the case on its active docket (Doc. 114), but the district court again denied the parties an opportunity to continue or resolve the litigation (Doc. 117). The case languished for another two years until finally, in response to letters by counsel for all parties, the district court held a status conference on June 16, 1997.

With leave of the district court, the plaintiffs filed their Seventh Amended Complaint on October 21, 1997 (Doc. 132) together with a motion pursuant to Rule 21 to add new plaintiffs (Doc. 131). There followed a new rash of the defendants' dismissal motions for lack of Article III subject matter jurisdiction pursuant to Rule 12(b)(1) and failure to state a claim pursuant to Rule 12(b)(6), and motions to deny the Rule 21 submission, among others. The district court issued a Memorandum Opinion and Order on June 25, 1998 denying the Rule 21 motion (Doc. 200) and a Memorandum Opinion and Order (Doc. 203) and Final Order of Dismissal (Doc. 204) on July 29, 1998 (entered July 30, 1998), dismissing for lack of Article III jurisdiction without reaching the merits. Having determined that it lacked subject matter jurisdiction to decide on the merits, the district court did not reach the merits of the Rule 12(b)(6) motions.

On November 8, 1999, the Fifth Circuit affirmed without opinion the judgment of the district court, stating only that the panel agreed that the district court had no subject matter jurisdiction.

REASONS FOR GRANTING THE WRIT

This case raises the question of how and when a plaintiff in a class action lawsuit under the securities laws should be considered the *de facto* plaintiff in place of a close family member. Perhaps more importantly, and a potential problem in any class action lawsuit, is the question of how and when a district court should decide on jurisdictional issues so that if a defect is found it can be cured in a timely manner so as not to disenfranchise an entire class.

This Court should grant certiorari in this case because the result of the district court's failure to act until many years after the case was first brought, and then only to dismiss the case entirely, was

to leave thousands of class members, who collectively lost hundreds of millions of dollars[2], with no further recourse. Moreover, while the courts below were satisfied to dismiss the entire litigation, courts in other cases have instead ordered class counsel to substitute a defective plaintiff with another member of the class in order to avoid throwing the case out altogether. Unless a clear guideline is pronounced, such an injustice is in peril of occurring again, even where, as here, the conduct of the defendants was egregious.

Krim Should Have Been Allowed to Litigate for His Son

The district court found, *in 1998*, that plaintiff Krim did not have standing to bring his complaint on July 16, 1990 because he was not at that time a purchaser of First City stock. Krim brought the original complaint based on the losses his family incurred by reason of the stock that was purchased in 1988 with Krim's money for the benefit of his minor child. This stock purchase was made pursuant to the Proxy Statement/Prospectus dated January 26, 1988 and through which First City underwent a restructuring and provided for the exchange of its old stock for a new issue. On paper, the actual purchase was made by Krim's wife; however, Krim argues that he was the *de facto* purchaser of the stock and thus the real party in interest.

Krim has also argued below that he was entitled under Fed. R. Civ. P. 17(a) to sue as a guardian on his son's behalf without having to join his son in the lawsuit. *Chuchuru v. Chutchurru*, 185 F.2d 62, 66-67 (10th Cir. 1950); *Bochantin v. Inland Waterways Corp.*, 9 F.R.D. 592 (E.D. Mo. 1950).

In addition, this Court has stated that a litigant may bring a case on behalf of a third party provided the litigant suffered an "injury in fact", the litigant has a close relationship with the third party, and there is some hindrance to the third party's ability to protect his own interests. *Powers v. Ohio*, 499 U.S. 400, 410-11 (1991); *Singleton v. Wulff*, 428 U.S. 106 (1976). These requirements are all met in this case:

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[2] As noted, *supra*, because the class members pursued their claims in the bankruptcy court where a partial settlement was reached of $11 million against the debtor only, the losses to the class are known and documented, and total approximately $375 million.

Krim has suffered an injury in fact by reason of a blow to his family's finances; the third party, Krim's son, is closely related to him; and the third party was unable to protect his own interests because at the time of the original lawsuit he was a minor.

Krim Was Himself Defrauded, and Should Have Been Deemed to Have Standing to Amend His Complaint

When Krim bought First City shares in his own name on July 19, 1990, none of the problems that continued into 1991 and 1992 at First City, briefly described *supra*, had yet been revealed. Thus, Krim was defrauded by the defendants' acts subsequent to his purchase. By the time of his first amended complaint, filed September 24, 1990, Krim was therefore a defrauded investor entirely in his own right irrespective of the earlier purchase for the benefit of his son. The wrongdoing took place over a period of years, and many elements, including defendant Cihak's conduct, were not known to Krim, the shareholders or the public in July 1990, but came out much later. Some activities were the subject of an undercover investigation by the U.S. Attorney's office in Houston, which culminated in the indictments against Cihak and others in April 1993 and August 1995, in which the facts were first revealed.

Krim's standing therefore should have been effected on his own behalf for the purposes of all the amended complaints filed after July 19, 1990. Instead, the district court has raised form over by asserting a blanket dismissal of the action based on Krim's lack of standing, without even addressing this aspect of the case. In fact, the district court made the following completely erroneous and insupportable conclusion in its Opinion:

> The amendments which reflect that Krim purchased shares of First City three days after he filed this lawsuit do not provide standing because Krim admittedly knew of the alleged fraud prior to the purchase.

(App., *infra*, 10a) This statement was blatantly, outrageously wrong, as the district court, and the court of appeals, should have recognized if they had read the pleadings in the case. While Krim knew of *some* of the fraud before his purchase, he did not and could not have known of fraud *that had not yet taken place.*

A thoughtful argument is favor of abandoning the

technicalities that deny the progress of a valid case is set forth in Circuit Judge Wisdom's dissent in *Summit Office Park, Inc. v. United States Steel Corp.*, 639 F.2d 1278 (5th Cir. 1981). In that antitrust case brought on behalf of a class of purchasers of fabricated reinforming steel bar (rebar) materials, the court affirmed summary judgment for the defendants on the grounds that the original plaintiffs were indirect purchasers of the rebar material and thus had no standing. The district court had also struck an amended complaint which attempted to substitute for the dismissed plaintiff two direct purchasers as plaintiffs and representatives of a new class. In his dissent, Judge Wisdom analyzes extensive case law holding, *inter alia*, that decisions on the merits should not be avoided on the basis of "mere technicalities", *Foman v, Davis*, 371 U.S. 178, 181 (1962); that an amended complaint adding a new plaintiff was a valid way to proceed, even though all of the original plaintiffs had to be dismissed, *Hackner v. Guaranty Trust Co.*, 117 F.2d 95 (2d Cir.), *cert. denied* 313 U.S. 559 (1941); that there is no particular magic in the way a claim for relief is instituted, *Chisolm v. Gilmer*, 299 U.S. 99 (1936); that as long as a defendant has had service "reasonably calculated to give him actual notice of the proceedings", the requirements of due process have been satisfied, *Milliken v. Meyer*, 311 U.S. 457 (1940). *Summit Office Park*, 639 F.2d at 1287-88. Judge Wisdom notes that where there is a valid complaint by "real, live plaintiffs" before the court, "the manner in which the complaint came before the court should be irrelevant unless it prejudices someone in some articulable way." *Id.* at 1286. Moreover, where, as in the instant case, an amended complaint could instead have been filed as a new action, "it is not easy to see who would have been prejudiced by accepting it as an amendment instead. Certainly not the defendants, who would be in the same position" as they would be if a new original complaint was filed. *Id.*

Recently, an analogous situation came before the United States District Court for the Southern District of New York. The plaintiff was held to be an inadequate representative of the class because units of stock he purchased were for his son, who was no longer a minor and had taken over the account his father had set up for him under the Uniform Gifts to Minor Act. Nevertheless, rather than summarily dismiss the class action for plaintiff's lack of standing, the court

ordered plaintiff's counsel to substitute another class member. *Baffa v. Donaldson, Lufkin & Jenrette Securities Corp.*, 185 F.R.D. 172, 174 (S.D.N.Y. 1999).[3]

In the instant case, the district court's elevation of form over substance with regard to Krim's claim, and doing so belatedly, has cost shareholders potentially hundreds of millions of dollars in losses that are now irretrievable.

The District Court Ignored the Issue of Krim's Standing Until It Became Too Late for the Class, and Misstated Its Own Orders

The district court's long delay before adjudicating the issue of Krim's standing is inexplicable. The defendants have been trying to have the case dismissed ever since it was first brought in 1990, and toward that end have made repeated motions to dismiss after each amendment to the complaint. The district court had ample opportunity to decide on Krim's standing as a plaintiff since, as noted in the Statement *supra*, in March 1991 the district court had before it, and denied, all the defendants' motions to dismiss up to that point. Petitioners here urge that the district court had a duty to determine subject matter jurisdiction at that point, particularly since, as the district court itself pointed out in its Opinion,

> The question of standing is so crucial that a court "is bound to ask and answer it for itself even when not otherwise suggested" by the parties.

(App., *infra*, 10a, *citing Steel Co. v. Citizens for a Better Environment*, 118 S. Ct. 1003, 1012 (1998).) The district court admitted that "the interests of justice are not served by disregarding constitutional requirements for federal court jurisdiction." (App., *infra*, 10a)

Here, the district court did not ask and answer the jurisdiction

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[3] The newly proposed plaintiffs were found to be inadequate as well, although for different reasons, and the motion to certify the class was denied as a result. The court also found that applications to intervene in the class action were time-barred. However, the new plaintiffs were permitted to intervene as individuals. *Baffa*, 185 F.R.D. at 178.

question for itself, not even when confronted several times with motions to dismiss. The district court's failure rendered ineffective this Court's ruling regarding the tolling of the statute of limitations in the class action context. *See American Pipe & Construction Co. v. Utah*, 414 U.S. 538, 552-53, 38 L. Ed. 2d 713, 94 S. Ct. 756 (1974) (held that commencement of a class action tolls the running of the applicable statute of limitations for all class members who upon denial of certification make timely motions to intervene); *Crown, Cork & Seal Co. v. Parker*, 462 U.S. 345, 350-52, 76 L. Ed. 2d 628, 103 S. Ct. 2392 (1983) (extending the tolling of the statute of limitations to those seeking to bring individual actions in the event class certification is denied, and to those electing to opt out of the class action in order to file individual claims). Thus, if the district court had considered Krim's standing early on, it could have come to one of two conclusions: either (1) Krim had standing, so even if his motions for class certification were denied the statute of limitations would have been tolled as to other class members, one or more of whom could have been substituted, *e.g.*, Harris, *American Pipe*, 414 U.S. at 552-53; or (2) Krim did not have standing and the case would have been dismissed, but another class member could have brought a new complaint even as late as 1994 because of the information that was coming out as late as 1993. 15 U.S.C. § 78. *Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson*, 501 U.S. 350, 363-64, 115 L. Ed. 2d 321, 111 S. Ct. 2773 (1991) (statute of limitations for cases under section 10(b) is three years from the violation and one year from the discovery of the violation); *Topalian v. Ehrman*, 954 F.2d 1125, 1135 (5th Cir.), *cert. denied*, 121 L. Ed. 2d 46, 113 S. Ct. 82 (1992). The district court's failure timely to determine Krim's standing foreclosed any other class member from pursuing the litigation.

Krim tried to have the district court consider at various times adding Harris or Krim's wife, Mead Ann Krim, or several other shareholders who came forth and were the subject of the plaintiffs' motion under Rule 21 to add plaintiffs, but the court refused to allow any of this. However, even though the court twice denied Krim's motions for class certification, it granted class certification in 1992, with Krim and Harris as class representatives, for settlement purposes. Either the district court failed again to consider Krim's standing at that time, or did not deem Krim's standing to be an impediment to

settlement.

The district court's actions were particularly unconscionable with respect to Harris. Krim added Harris to the Sixth Amended Complaint in May 1991 in direct compliance with an order of the court, which the court has since apparently misplaced, forgotten or both. Thus the district court's assertion in the conclusion of its Opinion that "Harris has never been properly added as a plaintiff in this case" is simply untrue. At least, if the district court considered the addition of Harris to the Sixth Amended Complaint improper, even though it was effected in order to comply with the court's own order, it should again have made that determination in 1991, not years and years later, in 1998 when it was too late to do anything about it. Inexplicably, the court of appeals completely ignored this issue.

The Questions Presented Are Important

Issues of standing affect every case brought in the courts of this country. So does the manner in which the presiding judge handles such issues. Petitioners respectfully urge this Court to certify this case in order to clarify the law in this area and pronounce a standard that all federal courts must follow to avoid such problems in the future.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,
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Counsel for Petitioner

February 2000

APPENDIX A

U.S. COURT OF APPEALS
FILED NOV 8, 1999
CHARLES R. FULBRUGE III

UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 98-20765

JERRY KRIM, Jerry Krim on behalf of himself and all other similarly situated, HAROLD L. HARRIS, individually and as Trustee of Mazel, Inc., Profit Sharing Plan,

Plaintiffs-Appellants,

VERSUS

FIRST CITY BANCORPORATION OF TEXAS, INC., ET AL.,

Defendants,

A. ROBERT ABBOUD, FRANK C. CIHAK, ROBERT D. RICHLEY, DONALDSON LUFKIN & JENRETTE SECURITIES CORP., C. IVAN WILSON, ROBERT W. BROWN, DANIEL C. ARNOLD, ROBERT RICE, ROBERT H. ALLEN, J. EVANS ATTWELL, WILLIAM T. BUTLER, M.D., J.A. ELKINS, JR., JAMES H. EVANS, C. JACKSON GRAYSON, JR., ROBERT N. MURRAY, RALPH S. O'CONNOR, MARGARET S. WILSON,

Defendants-Appellees.

Appeal from the United States District Court
for the Southern District of Texas
(H-90-CV-2269)

Before DAVIS, JONES and MAGILL[1], Circuit Judges.

PER CURIAM:**

After reviewing the record in this case and considering the briefs of the parties and their argument, we agree with the district court that it had no subject matter jurisdiction. Accordingly, we affirm the judgment of the district court essentially for the reasons stated in its July 30, 1998 Memorandum Opinion and Order.

AFFIRMED. All pending motions are hereby MOOT, in light of the opinion.

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[1] Circuit Judge of the Eighth Circuit, sitting by designation.

** Pursuant to 5TH CIR. R. 47.5, the Court has determined that this opinion should not be published and is not precedent except under the limited circumstances set forth in 5TH CIR. R. 47.5.4.

APPENDIX B

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF TEXAS
ENTERED JUL 30, 1998
Michael N. Milby, Clerk

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

JERRY KRIM and HAROLD L. HARRIS,	§	
Plaintiffs,	§	
	§	Civil Action No. 90-2269
v.	§	
	§	
A. ROBERT ABBOUD, *et al.*,	§	
Defendants.	§	

FINAL ORDER OF DISMISSAL

In accordance with the Memorandum and Order issued this day, it is hereby

ORDERED that this case is DISMISSED FOR LACK OF SUBJECT MATTER JURISDICTION.

Taxable costs are assessed against Plaintiff, Jerry Krim.

THIS IS A FINAL ORDER.

Signed this 29th day of July, 1998.

s/Kenneth M. Hoyt
KENNETH M. HOYT
United States District Judge

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF TEXAS
ENTERED JUL 30, 1998
Michael N. Milby, Clerk

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

JERRY KRIM and HAROLD L. HARRIS, Plaintiffs,	§	Civil Action No. 90-2269
v.	§	
A. ROBERT ABBOUD, *et al.*, Defendants.	§	

MEMORANDUM OPINION AND ORDER

This securities case is before the Court on Defendants' Motions to Dismiss (Instruments No. 147, No. 148, No. 151, No. 154, No. 158 and No. 161) and on Plaintiffs' Motion for Reconsideration (Instrument No. 201) of the Court's order entered June 25, 1998 (Instrument No. 200). The Court has carefully reviewed the applicable legal authorities and this entire record, including the thorough briefs submitted by the parties. Based on this review, the Court dismisses the complaint for lack of subject matter jurisdiction.

PROCEDURAL BACKGROUND

The procedural history in this case is extraordinary. On July 16, 1990, Plaintiff Jerry Krim ("Krim") filed his complaint alleging that First City Bancorporation of Texas, Inc. ("First City") and others violated sections 10(b), 10b-5 and 20 of the Securities Exchange Act of 1934 ("the 1934 Act") and sections 11, 12(2) and 15 of the Securities Act of 1933 ("the 1933 Act"). Three days later, Krim for the first time

purchased shares of First City stock for his own account.

On September 24, 1990, Krim filed an Amended Complaint. On September 26, 1990, Krim filed his Second Amended Complaint. On October 15, 1990, Defendants filed their motions to dismiss.

On October 25, 1990, Krim filed a motion for leave to amend and, on November 8, 1990, filed his Third Amended Complaint. Again, Defendants moved to dismiss and, again, Krim filed a motion for leave to amend. On January 11, 1991, Krim filed his Fourth Amended Complaint. Anticipating Defendants' motions to dismiss by one day, Krim filed his motion for leave to file a fifth amended complaint on January 24, 1991, and Defendants filed their motions to dismiss the Fourth Amended Complaint the next day. Krim filed his Fifth Amended Complaint on February 19, 1991. Defendants filed their motions to dismiss on March 1 and 6, 1991.

On March 26, 1991, the Court denied class certification. On May 9, 1991, the Court denied Krim's request for reconsideration. In the order denying reconsideration, entered May 10, 1991, the Court held specifically that Krim would not be a proper class representative. On May 24, 1991, without moving for or receiving leave of the Court and in violation of the court-ordered deadline of April 8, 1991 for joining new parties and amending pleadings, Krim filed his Sixth Amended Complaint. Named in the new complaint as a plaintiff was Harold L. Harris. Defendants filed their motions to dismiss the Sixth Amended Complaint.

Extensive discovery was conducted during the following year. In September 1992, the parties filed a joint motion for preliminary approval of a proposed settlement of the claims against First City. The parties proposed that the settlement be handled as a class settlement, and the Court concurred. Before the settlement was completed, however, First City filed for bankruptcy protection. The case was stayed and administratively closed.

While the case was stayed pending the completion of First City's bankruptcy proceedings, Defendants moved to have the stay lifted for the limited purpose of briefing, arguing, and obtaining a ruling on their motions to dismiss the Sixth Amended Complaint. Defendants' request was opposed by Krim and Harris. Approximately one year later, Krim and Harris sought to have the case reinstated as to the defendants other than First City. Because the

bankruptcy stay remained in effect as to First City, Defendants opposed proceeding with the case unless First City was dismissed.

In June 1997, the Court scheduled a status conference. At the conference, the Court reinstated the case and granted leave for Krim to file another amended complaint adding new defendants if necessary. Instead, on October 21, 1997, Krim filed his Seventh Amended Complaint, again naming Harris as a plaintiff and purporting to add other new plaintiffs.

Additionally, although the Court had twice denied class certification in this case and had conditionally approved the class only in connection with the proposed settlement, Krim and Harris included class action allegations in the Seventh Amended Complaint. Defendants moved to strike the class action allegations, and the Court granted their motion. Krim and Harris moved for reconsideration. All pending motions are now ripe for decision.

STANDARDS FOR DISMISSAL

Defendants have moved to dismiss the Seventh Amended Complaint under both Rule 12(b)(1) and Rule 12(b)(6) of the Federal Rules of Civil Procedure. In support of their 12(b)(1) motion, Defendants argue that Krim did not have standing when he filed his original complaint and does not have standing now because he cannot satisfy the causation requirement. In support of their 12(b)(6) motion, Defendants argue that Krim has failed to plead fraud with the particularity required by Rule 9(b) and that the claims are barred by the applicable statute of limitations.

Rule 12(b)(1) - Jurisdiction - The party asserting federal question jurisdiction bears the burden of establishing that it exists. *Steel Co. v. Citizens for a Better Environment*, 118 S. Ct. 1003, 1017 (1998). Standing to assert the claims raised in the complaint is an essential element of federal jurisdiction and must be determined as a threshold matter before resolution of the claims on their merits. *Id.* at 1012. "The requirement that jurisdiction be established as a threshold matter 'spring[s] from the nature and limits of the judicial power of the United States' and is 'inflexible and without exception.'" *Id.*, *quoting Mansfield, C. & L.M. Railway Co. v. Swan*, 111 U.S. 379, 382 (1884).

To establish that he has standing under Article III, Krim must

prove (1) that he has suffered "an injury in fact - a harm suffered by the plaintiff that is concrete and actual or imminent, not conjectural or hypothetical"; (2) "causation - a fairly traceable connection between the plaintiff's injury and the complained-of conduct of the defendant"; and (3) "redressability - a likelihood that the requested relief will redress the alleged injury. *Id.* At 1016-17 (citations omitted). Standing under federal securities laws "requires that a plaintiff be an actual 'purchaser' or 'seller' of securities who has been injured by deception or fraud 'in connection with' the purchase or sale . . . ." *7547 Corp. v. Parker & Parsley Development Partners*, 38 F.3d 211, 226 (5th Cir. 1994).

Rule 12(b)(6) - Failure to State a Claim - Rule 12(b)(6) provides for dismissal of a complaint in which the plaintiff fails "to state a claim upon which relief may be granted." Dismissal under Rule 12(b)(6) is appropriate when the complaint shows on its face that plaintiff cannot obtain the requested relief. *Clark v. Amoco Production Co.*, 794 F.2d 967, 970 (5th Cir. 1986). Under section 10(b) or Rule 10b-5, a plaintiff must prove: (1) a misstatement or omission; (2) of a material fact; (3) occurring in connection with the purchase or sale of a security; (4) that was made with scienter; (5) upon which the plaintiff justifiably relied; and (6) that proximately caused injury to the plaintiff. *Rubinstein v. Collins*, 20 F.3d 160, 166 (5th Cir. 1994). If the complaint shows on its face that a plaintiff cannot establish any one of these elements, dismissal is appropriate.

A complaint may also be dismissed when a plaintiff has failed to meet the pleading requirements of Rule 9(b) of the Federal Rules of Civil Procedure, which impose a heightened level of pleading for fraud claims. *Tuchman v. DSC Communications Corp.*, 14 F.3d 1061, 1067 (5th Cir. 1994). This requirement attempts to avoid the potential misuse of securities fraud litigation recognized by the United States Supreme Court in *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975). In *Blue Chip Stamps*, the Supreme Court noted that a complaint alleging federal securities law violations "which by objective standards may have very little chance of success at trial has a settlement value to the plaintiff out of any proportion to its prospect of success at trial so long as he may prevent the suit from being resolved against him by dismissal or summary judgment." *Id.* at 739-40.

Rule 12(b)(6) dismissal is appropriate where the complaint on its face establishes that the claims are barred by the statute of limitations. *Kansa Reinsurance v. Congressional Mortgage Corp.*, 20 F.3d 1362, 1366 (5th Cir. 1994). Claims under section 10(b) must be filed no later than one year after the discovery of facts constituting the violation and within three years after the alleged violations occurred. 15 U.S.C. § 78.

PURPORTED PLAINTIFF HARRIS

As described in the Procedural Background, Plaintiff Krim attempted to add Harold Harris as a plaintiff in the Sixth Amended Complaint. The Sixth Amended Complaint was filed without leave of the Court and in direct violation of the Court's April 8, 1991 deadline for adding new parties or amending pleadings. Consequently, the Sixth Amended Complaint has never been properly filed as a pleading in this case.

Following reinstatement of the case in 1997, Krim was granted leave to file a Seventh Amended Complaint adding any necessary new defendants. As stated herein and as held by the Court in its June 25, 1998, Order, leave was not granted to add new plaintiffs. Therefore, Harris was not properly added as a plaintiff in the Seventh Amended Complaint.

Because the Sixth Amended Complaint was not properly filed and because the Seventh Amended Complaint improperly attempted to add new plaintiffs, Harris is not a plaintiff in this case.

Moreover, Krim cannot amend his complaint to add Harris as a plaintiff. As discussed more fully below, Krim did not have standing at the time the original complaint was filed and does not have standing now. Where, as here, a plaintiff does not have standing upon which to base the Court's jurisdiction, he cannot amend to add new plaintiffs to create jurisdiction where none existed previously. *See Federal Recovery Services, Inc. v. United States*, 72 F.3d 447, 453 (5th Cir. 1995), *citing Aetna Casualty & Surety Co. v. Hillman*, 796 F.2d 770, 776 (5th Cir. 1986).

Harris has not been properly added as a plaintiff in this case. As a result, Defendants' motions to dismiss the claims purportedly asserted by Harris are moot.

PLAINTIFF JERRY KRIM

Krim, whom his attorney describes as "an experienced investor with a hugely diversified portfolio totaling millions of dollars," has claimed to be the victim of securities fraud by no fewer than three other corporations.[1] When he filed the original complaint against First City, Krim alleged that he "purchased shares of common stock of First City in 1988 . . . ." Krim has now admitted that the allegation is false. Krim's wife, not Krim, purchased shares of First City stock in 1988. Krim now admits that he did not purchase shares of First City stock until July 19, 1990, three days after he filed the lawsuit. Krim also admits that he purchased the First City stock with full knowledge of the fraud alleged in the complaint.

At the time the original complaint was filed, Krim did not have standing because he was not a purchaser of First City stock.[2] *See Blue Chip Stamps*, 421 U.S. at 731-33; *7547 Corp.*, 38 F.3d at 226. As discussed previously, "Rule 15 . . . do[es] not allow a party to amend to create jurisdiction where none actually existed." *Federal Recovery Services*, 72 F.3d at 453, *quoting Hillman*, 796 F.2d at 776.

Additionally, Krim's amended complaints failed to establish Article III standing. Although by the time the second amended

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[1] Krim has filed complaints alleging securities fraud against Browning-Ferris Industries, Inc. in the Southern District of Texas, against BancTexas Group, Inc. in the Northern District of Texas, and against Crazy Eddie, Inc. in the Eastern District of New York.

[2] Krim argues that he should be regarded as the purchaser of the stock his wife bought in 1988 because she used his money. This argument is without merit, however, because the proper plaintiff in a federal securities case is the "actual purchaser . . . of securities who has been injured . . . ." *7547 Corp.*, 38 F.3d at 226. Krim was not the "actual purchaser" of the shares in 1988. Additionally, it would be the owner of the shares, not Krim, who was "injured" in connection with that purchase by a diminution in the value of the stock. *See Fuchs v. Swanton Corp.*, 482 F. Supp. 83, 88-89 (S.D.N.Y. 1979).

complaint was filed, Krim was a "purchaser," he has admitted that he purchased the stock with full knowledge of the alleged fraud. As a result, he cannot establish the causation requirement for standing. There can be no fairly traceable connection between Krim's injury in connection with the purchase of his stock and the alleged fraud. One cannot be defrauded when he knows the representations or omissions are fraudulent. *Roberts v. United New Mexico Bank at Roswell,* 14 F.3d 1076, 1081 (5th Cir. 1994).

Krim argues that he should be permitted to proceed with this case, indeed to represent a certified class of plaintiffs, because he believes that would serve the interests of justice. Standing is an essential of the case-or-controversy limitation on federal court jurisdiction contained in Article III of the United States Constitution. *Lujan v. Defenders of Wildlife,* 504 U.S. 555, 560 (1992). The question of standing is so crucial that a court "is bound to ask and answer [it] for itself, even when not otherwise suggested" by the parties. *Steel Co.,* 118 U.S. at 1012. For a court to consider the claims under federal law "when it has no jurisdiction to do so is, by very definition, for a court to act *ultra vires.*" *Id.* at 1016. The interests of justice are not served by disregarding constitutional requirements for federal court jurisdiction.

MOTION TO RECONSIDER

Krim has filed a motion for reconsideration of the Court's June 25, 1998 Opinion and Order denying amendment to add new plaintiffs and striking the class allegations. For the reasons set forth in the June 25 Order, and for the reasons stated herein regarding Krim's lack of standing, the Court concludes that its prior decision was correct and reconsideration is denied.

CONCLUSION AND ORDER

Krim did not own First City stock and did not have standing when he filed the original complaint in this case. As a result, he cannot amend to create jurisdiction where none previously existed. The amendments which reflect that Krim purchased shares of First City three days after he filed this lawsuit do not provide standing because Krim admittedly knew of the alleged fraud prior to the

purchase.

Harris has never been properly added as a plaintiff in this case. Moreover, because Krim does not have standing, he cannot amend to add new plaintiffs.

Standing is an essential element of the case-or-controversy requirement of Article III and, absent standing, the case must be dismissed for lack of jurisdiction. Accordingly, it is hereby

ORDERED that this case is DISMISSED FOR LACK OF SUBJECT MATTER JURISDICTION (Instruments No. 147, No. 148, No. 151, No. 154, No. 158 and No. 161). Plaintiffs' Motion for Reconsideration (Instrument No. 201) is DENIED.

Signed this 29th day of July, 1998.

s/Kenneth M. Hoyt
KENNETH M. HOYT
United States District Judge

APPENDIX C

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF TEXAS
ENTERED MAR 28, 1991
Jesse E. Clark, Sr. Deputy

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

JERRY KRIM, ON BEHALF OF HIMSELF AND ALL OTHERS SIMILARLY SITUATED,	§	
Plaintiffs,	§	
v.	§	Civil Action No. 90-2269
FIRST CITY BANCORPORATION OF TEXAS, INC., ET AL.,	§	
Defendants.	§	

ORDER

The following motions are disposed of in the following manner:

(a) the defendants' motions to dismiss (instruments 8 and 9) are DENIED;

(b) the plaintiff's motion for class certification (instrument #34) is DENIED. The Court is not convinced that each putative plaintiff was injured, or for that matter was injured by the same conduct. Moreover, a hearing on class certification would require the testimony of numerous potential plaintiffs

resulting in a mini-trial. Therefore, the Court ORDERS that the plaintiff produce the names of all plaintiffs who are parties or have expressed a desire to be a plaintiff. The issue is not whether fraudulent representation occurred, but whether anyone relied upon the representations to their detriment.

(c) The defendants' motion to dismiss plaintiff's fourth and fifth amended complaint (instrument #37, 46, and 49) are DENIED without prejudice and the need to refile same. In this regard, the plaintiff is ORDERED to file a Sixth Amended Complaint, within 60 days expressly satisfying the particularities required to establish a claim for securities fraud and for claims under the Securities Act of 1933 or the Securities Exchange Act of 1934. The plaintiff should be mindful of FRCP 11 in this instance.

No response to the motions to dismiss is required unless the plaintiff is of the opinion that the fifth amended complaint is sufficient and desires that the Court make its ruling based upon that pleading.

Signed this 26th day of March, 1991.

s/Kenneth M. Hoyt
KENNETH M. HOYT
UNITED STATES DISTRICT JUDGE